EXMINIT NO. 5

BATE 1.8.09

BALL NO. - NO.-



Senate Taxation Committee
January 8, 2009

1

Total Corporate Income – Federal Income Tax

Gross Receipts or Sales

Less: Cost of Goods Sold

Equals: Gross Profit

Plus: Dividends, Interest

Gross Rent Gross Royalties

Capital Gains

Supplemental Gains

Other Income

Equals: Total Income

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Federal Taxable Income

Total Income

Less

Compensation of Officers
Wages and Salaries
Pension, profit sharing plans, etc.
Employee benefit program costs
Repairs, maintenance
Bad debts
Rents and interest paid
Taxes and licenses
Charitable contributions

Charitable contributions

Depreciation, depletion

Advertising and other deductions

Equals:

Federal Taxable Income

3

Montana Corporation License Tax - Starting Point

The starting point for Montana's Corporation License Tax is:

Federal Taxable Income (FTI)

Federal law controls all of the income and deduction items discussed previously



- Montana corporation license tax included in FTI
- Other state, local, foreign and franchise taxes (based on income)
- Federal tax exempt (municipal) interest
- Contributions used to compute Montana's charitable endowment credit
- Other additions (e.g. extraterritorial income exclusion, capital loss carryover)

MT Subtractions from FTI

- IRC "Section 243" dividends received deduction
- Nonbusiness income
- Montana recycling deduction
- Other reductions (e.g. current year capital losses must be deducted in year incurred)



Federal Taxable Income

Plus: Montana Additions

Less: Montana Subtractions

Equals: Adjusted Federal Taxable

Income

Approach – General

Corporations operating in more than one state must have their income apportioned to each of the states in which they operate.

Montana apportions income of multistate corporations using the traditional Uniform Division of Income for Tax Purposes Act (UDITPA) equally-weighted, 3factor apportionment formula.



The UDITPA three factors used to apportion income under this approach are:

- PROPERTY (Original Cost)
- > PAYROLL
- > SALES

Apportionment Factor -Example Example Calculation of Apportionment Factor for Multistate Corporporation Factor Montana MT Factor **Property Factor** \$2,500,000,000 \$223,000,000 0.0892 **Payroll Factor** \$327,000,000 \$16,000,000 0.0489 Sales Factor 0.0755 \$1,298,000,000 \$98,000,000 0.2136 Sum of Montana Factors: Apportionment Factor (sum of MT factors divided by 3):



Adjusted Fed Taxable Income

Times: Apportionment Factor

Equals: Apportioned MT Income

Plus: Income Allocated Directly

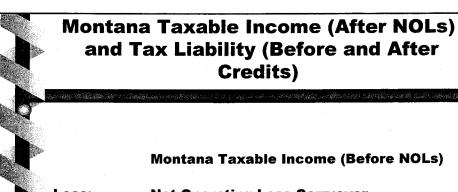
to Montana

Equals: Montana Taxable Income

(before net operating losses)

Net Operating Losses

- In simple terms, a net operating loss (NOL) is the excess of deductions over gross income in any tax year
- Corporations may reduce taxable income in previous or subsequent tax years by carrying forward or carrying backwards net operating losses
- Net operating losses may be carried back for 3 tax periods
- Net operating losses may be carried forward for 7 tax periods



Less:

Net Operating Loss Carryover

Equals:

Montana Taxable Income (After NOLs)

Times: Equals: 6.75% (7% if "Water's Edge" Corporation)

Tax Liability Before Credits

Less:

Tax Credits

Equals:

Tax Liability After Credits

13

Tax (Refund) Due at Time of Filing

Corporations may owe tax or be due a refund at the time of filing:

Tax Liability After Credits

Less:

Prior Year Overpayments

Tentative Payments

Quarterly Estimated Tax Payments

Equals:

Net Tax (Refund) due



- States may require corporations to file on either a unitary (combined) or separate reporting basis
- Montana is a worldwide, combined unitary state and unitary corporations must apportion income as provided for in 15-31-305, MCA

15

Unitary (Combined) Reporting

Business is unitary when:

- 1) Operation within the state is dependent upon or contributory to operations outside the state, or
- 2) Units of the business within and without the state are closely allied or incapable of separate maintenance

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Unitary (Combined) Reporting

Unitary requirements ("three-unities" test):

- 1) Unity of ownership (affiliate owned greater than 50%, control established)
- 2) Unity of operation (economies of scale centralized staff functions purchasing, advertising, human resources, etc.); and
- 3) Unity of use (centralized executive force making decisions regarding strategy and operations, intercompany transfer of products, know-how and expertise)



Separate Company Reporting

- Each member of a commonly controlled group computes income and files a return as if it were a separate economic entity
- Provides opportunities to create legal structure and intercompany transactions to shift income from affiliates in high-tax states to affiliates in low-tax states



"Water's Edge" Corporations



- Available only to multinational corporations
- Allows exclusion of corporations operating almost exclusively outside US (80% rule)
- Three-year renewable election
- Tax Rate of 7% (rather than 6.75%)

19



Audit Program (RARs)



15 Corporation Tax Auditors





 Field Audits (Review filing methods, large nonbusiness deductions, apportionment factors, etc.)